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No. 83-737

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA & THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Appellants,

vs.

UNITED STATES OF AMERICA, *et al.*,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

MOTION TO AFFIRM OF APPELLEE PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA

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necessary that he make a public interest determination on the proposed MFJ, J.A. 148-149, but that the Tunney Act required that he retain jurisdiction and insist, as a condition of approval of the MFJ, that it be amended to also require the Court's approval of the plan of reorganization. J.A. 156. As a result, Judge Greene decided to make the Tunney Act decision in two stages; first he would decide whether the MFJ was in the public interest, and, second, he would decide if the plan of reorganization conformed to his initial determinations so as to likewise be in the public interest.

In his August 12, 1982 order, Judge Green examined the issue of debt distribution as part of his overall consideration of the division of assets and liabilities.[3] J.A. 133-138. Questions were raised as to the appropriate debt-equity ratios, and Judge Greene accepted the suggestions of A.T.&T. and the Department of Justice that A.T.&T. divest the BOCs with debt-equity ratios of approximately 45% and assume its representative share of outstanding debt. Judge Greene interpreted his Tunney Act duties to require that the debt distribution proposal be made a part of the MFJ, so he would be in a position, if necessary, to insist that the statements of intention were actually implemented. J.A. 137.

As part of his consideration of the debt issue, Judge Greene pointed out that Pacific's debt-equity ratio was around 75%, substantially higher than the Bell System

[3]Given the fact that 22 BOCs were being separated from the Bell System and the fact that the Bell System had been highly integrated, the intervenor parties and Judge Greene were concerned about both the multiplicity of decisions to be made and the risk that the parent would manipulate the division of assets and liabilities to its benefit and the BOCs' detriment.

tion of the public interest determination which was required by the Tunney Act. As a result, this Court's role in this appeal is to review the public interest determination. The only case discussing the scope of an appellate court review of a Tunney Act public interest determination suggest that the appellate court's role is extremely limited; it is primarily to assure itself that the district court applied the proper Tunney Act standard and procedures. See *United States v. Bechtel,* 648 F.2d 660 (9th Cir. 1981). Once the District Court has applied the proper standard and has followed required procedures, its decision to approve a settlement under the Tunney Act is essentially discretionary; there is nothing in the reported decisions or the Tunney Act's legislative history to suggest tht the reviewing court's standard is other than the abuse of discretion standard normally applied in such situations.[6]

B. California's Lack of Equity

The cost of debt that the plan of reorganization provides for Pacific is entirely proper under the circumstances of the case. The objections of California to that cost of debt lack merit, and, therefore, this Court should summarily affirm the decision of the District Court to divest

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[6] *United States v. Bechtel, supra* is the only reported court of appeals decision reviewing a Tunney Act public interest determination. There are numerous district court decisions in addition to Judge Greene's August 12, 1982 opinion, J.A. 26-36 which examine the standard to be applied by a district court in deciding whether to accept a settlement. See, e.g., *United States v. Carrols Dev.Co.,* 454 F. Supp. 1215, 1222 (N.D.N.Y. 1978); *United States v. National Broadcasting Co.,* 449 F. Supp. 1127, 1143 (D.D. Cal. 1978); *United States v. Gillette Co.,* 406 F. Supp. 713, 716 (D. Mass. 1975). The legislative history of the Tunney Act is at 1974 U.S.Cong. Code & Admin. News 6535 (HR 93-1463).

Pacific with an average cost of funded debt of approximately 9.5%.

At least two reasons, having to do with economic growth and utility regulatory policy in California, justify the decision of the District Court. First, California, like the rest of the Sunbelt, has experienced a faster rate of growth than have other parts of the Country. Plan at 194-195. That faster growth rate has caused greater utility plant construction. As a consequence, BOCs in the Sunbelt, like Pacific, have issued debt more recently and more frequently than have BOCs serving slower growth areas. Since the cost of debt has risen in recent years, the average cost of debt of the Sunbelt BOCs has been higher than that of other BOCs. *Id.* California concedes that Pacific has had significant capital needs recently and that the lack of equity investment in Pacific has meant massive high cost debt. California Preliminary Comments at 23.

Second, there is considerable evidence in the record to show that utility regulatory policies in California may have led to higher costs of debt for Pacific than even for other Sunbelt BOCs, much less non-Sunbelt BOCs. See A.T.&T. Response at 285-298. California maintains that AT&T has refused to invest equity in Pacific, California Preliminary Comments at 15, but has not explained just why this is so. And AT&T has referred to a planned equity offering in 1979 of 10,000,000 shares of Pacific that the BOC aborted on the advice of the BOC's investment bankers because its earnings record made the offering impossible on reasonable terms. AT&T Response at 291-292. California has not replied to this point.

Thus it has come to pass that the cost of debt varies among the BOCs, with Pacific having the highest such cost. The District Court clearly recognized that this might be the case when it stated that

> The Court expects that the plan of reorganization will provide each Operating Company with a debt portfolio that reflects the terms and conditions comparable to the debt held by the Bell System as a whole unless it can be shown that, with respect to a particular Operating Company, its own current debt provides a more equitable basis.

(J.A. 137 n.321)

Furthermore, Section VIII(H) of the MFJ provides that equalization of debt costs may yield to exceptions. J.A. 185. The basis for an exception, of course, would be that the equities warrant the grant of an exception. See J.A. 137 n.321. It is abundantly clear that the equities militate against California's request for a 9.2% cost of debt. Rather, quite to the contrary, they point to a higher cost of debt for Pacific than for other BOCs.

The fundamental problem is that to grant California's request will mean that someone else will have to bear the expense represented by the difference between servicing debt at a cost of 9.2% and servicing it at a cost of 9.5%. The question is who that someone else is. California says that spreading Pacific's high debt cost does not have to "significantly disadvantage" any BOC and that the burden of Pacific's debt can fall "primarily" on AT&T. California Preliminary Comments at 25. California later claimed that matters can be arranged so that AT&T alone would bear the burden of reducing Pacific's debt cost. California Reply Comments at 9.

It is not clear that the other BOCs can be insulated from the adverse effects that would result from spreading Pacific's high cost of debt. If AT&T's costs must increase in order to satisfy California's demand for lower debt cost, it

may well be that ratepayers in the District of Columbia and elsewhere will have to pay higher rates to AT&T.

Furthermore, California first represented to the District Court that the other BOCs would in fact suffer some disadvantage. California Preliminary Comments at 25. Leaving aside the problems of which representation to believe, it seems altogether probable that AT&T would not feel bound to shoulder the entire burden by itself and would therefore share the burden with other BOCs or that the district court, on a remand, would effect such a result.

California has claimed, in effect, that Pacific's high debt cost is AT&T's fault. It has not proved that allegation[7] and it has not established, therefore, any reason why AT&T should not be allowed to place some or all of the burden that California wishes to impose on AT&T on other BOCs.

California has failed to demonstrate that other BOCs and their ratepayers must suffer the consequences of Pacific's high cost of debt. Nothing in the record in this case remotely suggests that ratepayers in the District of Columbia or the BOC there, for exmaple, are responsible for the differential in the rates of economic development in California and the Sunbelt on the one hand and growth in other parts of the country. Nothing in the record supports the notion that District of Columbia ratepayers or the BOC that serves them drove equity investors away from Pacific.

The District Court quite correctly and properly concluded that low growth areas of the country should not subsidize high growth areas. J.A. 221-222 n.64. Furthermore,

[7]If anything, AT&T has proved the contrary. See AT&T Response at 285-298.

while the District Court retreated somewhat from the conclusion that California regulators drove up Pacific's cost of debt, compare J.A. 137 n.320 to J.A. 221 n.64, the fact remains that the record shows that the investment community so believed, see AT&T Response at 285-298, and, therefore, the impact of Pacific's cost of debt was the same that would have resulted if the California regulators had forced up that cost. At the very least, California failed to dispel the supposed misimpression concerning its regulatory policies affecting Pacific.

Furthermore, California has already managed to get AT&T to agree to a 46.5% debt-equity ratio rather than the 50% ratio earlier authorized by the District Court, see J.A. 137 n.320, J.A. 184, and an average cost of funded debt of 9.5%, which is apparently lower than actual pre-divestiture cost. See California Reply Comments at 7-8. The effect of these concessions is necessarily to shift the burden of some of Pacific's high costs elsewhere. Yet no one has complained of that fact. California's desire for even more, under the circumstances, should not be satisfied.

Finally, it appears that Southwestern Bell's cost of debt has increased from 9.1% to 9.4%. See Plan at 194; AT&T Motion to Affirm at 22. Thus California is seeking a lower cost of debt than that that Southwestern Bell will have to carry, even though no one has complained in this proceeding about the policies of those who have regulated Southwestern Bell over the past few years or about that BOC's cost of debt. There is nothing in the record that can support a further reduction in Pacific's cost of debt from 9.5% to 9.2% in the face of Southwestern Bell's current cost of 9.4%.

The equities line up solidly against California. California has not shown that Pacific's cost of debt is the fault of

QUESTION PRESENTED

Whether the District Court violated the Tunney Act, 15 U.S.C. §16, when, after approval of the settlement of the A.T.&T. antitrust case, the District Court approved the plan of reorganization of the Bell System without requiring that the average cost of long-term funded debt retained by Pacific Telephone & Telegraph Company ("Pacific") be reduced to the average of the Bell system.

The D.C. Commission regulates local telephone rates and services in the District of Columbia. As such, it has jurisdiction over The Chesapeake & Potomac Telephone Company, which is presently a Bell System operating company ("BOC"). The D.C. Commission was a party below and, pursuant to Rule 10.4, is an appellee in this appeal. Its primary interest in this appeal is brought about by the possibility that part of Pacific's high cost debt will be distributed to other BOCs and, as a result, burden local ratepayers in the District of Columbia. For that reason, it is interested in the second question presented in the jurisdictional statement filed by the People of the State of California and the Public Utilities Commission of California (collectively referred to as "California"). The D.C. Commission moves the Court to affirm as to that issue.[1]

STATEMENT OF THE CASE

Following the parties' settlement agreement in *United States v. American Telephone & Telegraph Co.*, Judge Greene, who was presiding over that case, ruled that he would follow the Tunney Act, 15 U.S.C. §16, in deciding whether to accept the settlement. J.A. 25.[2] There were ex-

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[1]The D.C. Commission takes no position regarding the first issue, which is presented by both California and by the appellant in No. 83-738.

[2]Judge Greene never flatly ruled that he was required to follow the Tunney Act. See J.A. 19-22, 25 n.66. The parties, however, acquiesced in Judge Greene's following the Tunney Act, J.A. 22, and, in the appeals from his August 24, 1983 modification of final judgment ("MFJ") no party contended that Judge Greene had erred in following the Tunney Act. As a result, the applicability of the Tunney Act is the law of the case. It should be noted, however, that, although Judge Greene did not technically rule that the Tunney Act had to be followed, he made clear his view that it had to apply and that a public interest determination had to be made. J.A. 20-21.

tensive Tunney Act proceedings, after which Judge Greene entered an order on August 12, 1982, J.A. 1, ruling that, in the event the parties made certain significant changes in the settlement agreement, he would approve the settlement. The settlement agreement actually involved a dismissal of the then-pending government antitrust charges in *United States v. American Telephone & Telegraph Co.*, D.D.C. C.A. No. 74-1698, and a modification of the final judgment in *United States v. Western Electric Co.*, D.D.C. C.A. No. 82-0192. In the latter case, there had been a 1956 consent decree in a government antitrust case commenced in 1949 which, as part of the 1982 settlement review procedures, was transferred to the District of Columbia for consolidation. Judge Greene's required changes dictated amendments of the modification of the final judgment ("MFJ") in *Western Electric* to which the parties had agreed.

In view of the magnitude of the case and the numerous issues presented by the settlement, Judge Greene was faced with varous alternatives as to how and when to make the public interest determination contemplated by the Tunney Act. Under the settlement agreement, the government and A.T.&T. contemplated entry of an MFJ to be followed six months later by A.T.&T.'s filing of a detailed plan of reorganization for Department of Justice review. The Department of Justice and A.T.&T. viewed the Court's role as limited to review of the MFJ, leaving approval of the plan of reorganization to the Department of Justice. Many of the intervenor parties, however, argued that it was impossible to make a proper Tunney Act public interest determination without the plan of reorganization before the Court and that Judge Greene should defer final approval until he had the plan of reorganization before him. J.A. 147-148. Judge Greene concluded that it was

average, due to actions of California's regulators. J.A. 1378 n.320. Judge Greene ruled that he would accept a reduction of Pacific's debt to 50%. *Id.* He then added, as a required modification, the following provision:

> H. At the time of the transfer of ownership provided for in section I(A)(4), the separated BOCs shall have debt ratios of approximately forty-five percent (except for Pacific Telephone and Telegraph Company which shall have a debt ratio of approximately fifty percent), and the quality of the debt shall be representative of the average terms and conditions of the consolidated debt held by A.T.&T., its affiliates and the BOCs at that time. Upon application by a party or a BOC, the Court may grant an exception to this requirement.

The parties accepted the required changes in the MFJ and, as a result, Judge Greene entered the MFJ on August 24, 1982. There were several appeals. After Judge Greene certified them to this Court under the Antitrust Expediting Act, 15 U.S.C. §29, the Court summarily affirmed on February 22, 1983. *Maryland v. United States,* ___ U.S. ___, 103 S.Ct. 1240 (1983). One of the issues raised in the appeal was the validity of the public interest standard which Judge Green had applied. The Court wrote no opinion, but it is clear that the matter was before the Court and considered, because it is discussed in the opinion of three Justices dissenting from summary affirmance. No appellant complained about Judge Geene's decision to continue the public interest determination process into a review of the plan of reorganization or the substantive decision to approve the proposed debt-equity ratio but to make it part of the MFJ.

In the meantime, approval of the plan of reorganization was conducted in two stages; Judge Greene would first ex-

amine the reconfiguration of the long distance network[4] and then review the division of assets and liabilities. J.A. 195. In both instances, he used the same decisional mechanism; he indicated what changes he would require of the parties as a prerequisite to his approval of the relevant portion of the plan of reorganization.

In his July 8, 1983 order setting out the changes that he would require in the plan of reorganization, Judge Greene demanded significant changes in such important matters as ownership of trademarks and patent licensing because of his analysis of the public interest. California complained about the part of the plan of reorganization which distributed debt to Pacific, arguing that Pacific should not be given long term debt which had a higher cost of servicing than the Bell System average. Judge Green rejected this claim together with several others relating to liabilities and debt, but he did not specifically discuss his analysis of California's claim. J.A. 221, n.64.

SUMMARY AFFIRMANCE

A. The Legal Standard

Under the Antitrust Expediting Act, 15 U.S.C. §29, this Court's role is essentially the same as that which a court of appeals would have served if the district court had not certified direct appeal.[5] As indicated earlier, Judge Greene's review of the plan of reorganization was really a continua-

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[4]Order of April 20, 1983, not included in J.A.

[5]See *United States v. duPont deNemours & Co.*, 366 U.S. 316, 321-325 (1961); *Int'l. Boxing Club v. United States*, 358 U.S. 242, 253 (1959).

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

TABLE OF AUTHORITIES iii

MOTION TO AFFIRM 1

STATEMENT OF THE CASE 2

SUMMARY AFFIRMANCE 6

A. The Legal Standard 6

B. California's Lack of Equity 7

CONCLUSION 12

TABLE OF AUTHORITIES

Cases: Page

Int'l. Boxing Club v. United States,
358 U.S. 242 (1959) 6

Maryland v. United States,
____ U.S. ____, 103 S.Ct. 1240 (1983) 5

United States v. Bechtel,
648 F.2d 660 (9th Cir. 1981) 7

United States v. Carrols Dev. Co.,
454 F. Supp. 1215 (N.D.N.Y. 1978) 7

United States v. duPont deNemours & Co.,
366 U.S. 316 (1961) 6

United States v. Gillette Co.,
406 F. Supp. 713 (D. Mass. 1975) 7

United States v. National Broadcasting Co.,
449 F. Supp. 1127 (C.D. Cal. 1978) 7

Statutes:

Antitrust Expediting Act, 15 U.S.C. §29 6

Tunney Act, 15 U.S.C. §16 7

Legislative History:

1974 U.S. Code, Cong & Admin. News 6535 7

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MOTION TO AFFIRM

Appellee Public Service Commission of the District of Columbia ("the D.C. Commission") moves the Court pursuant to Rule 16(c) to affirm the judgment sought to be reviewed on appeal on the ground that it is manifest that the question on which the decision of the cause depends is so insubstantial as not to need further argument.

AT&T. Therefore, neither AT&T nor any of the other BOCs should be asked to take on any more of Pacific's costs than AT&T has previously agreed to do. In addition, the actions taken by AT&T to date regarding Pacific's debt-equity ratio and debt cost have markedly enhanced Pacific's future prospects. See J.A. 221-222 n.64. No credible basis exists, therefore, for the further relief sought by California.

CONCLUSION

The Court should summarily affirm.

Respectfully Submitted,

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December 7, 1983